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on 15 March 1955. Concurring were the Special Assistant, Intelligence, Department of State; the Assistant Chief of Staff, G-2, Department of the Army; the Director of Naval Intelligence; the Director of Intelligence, USAF; and the Deputy Director for Intelligence, The Joint Staff. The Atomic Energy Commission Representative to the IAC and the Assistant to the Director, Federal Bureau of Investigation, abstained, the subject being outside of their jurisdiction.

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PROBABLE DEVELOPMENTS IN BRAZIL

THE PROBLEM

To estimate the current situation in Brazil and probable developments through 1955.

CONCLUSIONS

1. The suicide of President Vargas in August 1954 and succession of the moderate-conservative Cafe Filho administration have not resulted in any fundamental change in the Brazilian situation. The economic situation remains precarious. Inflation continues largely unabated and the persistent dollar shortage is being met only by successive US loans. The political situation is affected by persistent social unrest, particularly in urban areas, and is aggravated by uncertainties relating to the presidential election to be held in October 1955. *(Paras. 11, 20, 44)*

2. The new president to be elected in October is likely to be a man committed to meet labor-leftist demands, assuming that free elections are held. The strongest labor-leftist candidate is Juscelino Kubitschek, governor of Minas Gerais and a former adherent of Vargas. The election of such a man is likely to create a political situation similar to that which existed under the Vargas regime; i.e., chronic political tension between the executive and moderate-conservative elements, in Congress and especially in the armed forces. The military would be confronted with a hard choice between condoning further evolution to the left or immediately imposing a government to their liking. *(Paras. 23, 26)*

3. A moderate-conservative could be elected in a free contest only if the labor-leftist vote were seriously split. Such a candidate, elected with multiparty backing and the approval of the military, could probably enlist sufficient congressional cooperation to effect some improvements in the economic situation. A moderate-conservative regime would be unlikely to antagonize politically vocal conservative elements, and would be in a position to employ force, if necessary, to suppress social unrest. *(Paras. 21, 24, 25)*

4. There is little chance that the administration to be elected in October will be able to deal effectively with Brazil's deep-seated and politically dangerous economic difficulties. In fact, as long as any Brazilian administration assumes that dollar loans are readily available, there is little likelihood that it will incur the political

risk involved in stabilizing the economy. However, the administration would be even less willing to follow politically dangerous policies in the absence of dollar loans. Rather, it would be under extreme pressure to seek radical, nationalistic solutions to Brazil's economic problems. In any case, effective action over an extended period will be required to stabilize the Brazilian economy. *(Para. 47)*

5. The Brazilian Communist Party, although outlawed, has approximately doubled in numbers during the last two years. It is now estimated to have 100,000–120,000 members and a much larger number of sympathizers. For some time to come, it will probably continue to increase in numbers and political influence. It is unlikely, however, that the party could, within the foreseeable future, gain sufficient strength to take control of Brazil by electoral means or by force. *(Paras. 27, 34)*

6. Brazil will almost certainly continue to support the US on major issues between the US and the Soviet Bloc, but, if not granted the special consideration to which it feels entitled, with particular reference to dollar loans, may pursue an increasingly independent course. Brazil will seek to establish closer economic relations in Latin America and with Western Europe, and will also seek to increase its now minor nonstrategic trade with the Soviet Bloc. *(Para. 57)*

7. Brazil will continue to oppose Argentine bids for leadership in Latin America and the development of an Argentine-led bloc. Fundamentally, Brazil deprecates the idea of competing blocs in Latin America and promotes instead the concept of Hemisphere solidarity. *(Para. 55)*

8. In the event of general war, Brazil would almost certainly participate actively in support of the US. *(Para. 56)*

DISCUSSION

I. INTRODUCTION

9. Brazil is a major power within the Latin American community. It exercises considerable influence in both the Organization of American States and the United Nations. Moreover, Brazil is strategically located with respect to sea and air routes in the South Atlantic and is an important source of strategic materials, notably metallurgical manganese, quartz crystals, beryl ore, mica, tungsten, tantalite, and castor oil. It is the only Latin American country with known sizeable deposits of atomic energy raw materials, principally thorium. The Brazilian armed forces are capable of making an important contribution to Hemisphere defense. Traditionally, Brazil has cooperated closely with the United States on important international questions.

10. Except in some geographical areas (e.g., Sao Paulo) little progress has been made in developing Brazil's large human and material resources. The national economy continues to depend on exports of agricultural products. Earnings from these exports have not been sufficient to sustain the postwar rate of industrial development, while at the same time economic nationalism has impeded foreign investment. The industrialization which has occurred since 1930 has been accompanied by severe inflation and by economic and social strains felt particularly by the rapidly growing urban population.

11. Heavy migrations from the back country into the cities have brought hundreds of thousands of Brazilians into their first contact with higher standards of living, glaring

inequalities, and the insecurity of urban existence. Acutely distressed by inflation, the urban masses generally are increasingly dissatisfied with their level of living and clamorous for improvement. At the same time middle and upper class conservatives, including Army leaders as well as commercial and industrial interests, have been disturbed by the adverse prospects for maintaining a high rate of economic development and by the growth of labor-leftist and Communist strength, which threatens their dominant position in Brazilian life. The conflicts and tensions which inevitably arise in such time of rapid economic and social change are continuously exploited in Brazil by both extreme nationalists and Communists. Brazil, however, has been less subject to political violence than most Latin American countries.

II. THE POLITICAL SITUATION AND PROSPECTS

The Collapse of the Vargas Regime

12. The present administration came to power in August 1954 as a result of the suicide of President Getulio Vargas. The Vice-President, Joao Cafe Filho, thereupon succeeded constitutionally to the presidency for the remainder of Vargas' term (until 31 January 1956). An understanding of the character of the Vargas regime and the causes of its collapse is prerequisite to an estimate of the present political situation and prospects.

13. Vargas was an astute politician who shrewdly manipulated opposing factions and successfully posed as the friend of the common people. During his first period in power (1930–1945) he established the quasi-fascist "New State" as an ideological facade for his strong personal rule. He espoused cultural and economic nationalism, established federal control over the states, abolished political parties, suppressed all opposition of both the left and right, undertook government intervention and initiative in economic development, promoted industrialization, concerned himself with amelioration of the living conditions of the urban masses, extended the franchise, and sought to mobilize and control urban labor as a political force through government-sponsored labor unions. It was during this period that urban lower income groups began to become an important factor in Brazilian politics.

14. In 1945, in response to a growing opposition to totalitarianism, the Brazilian Army quietly deposed Vargas and established a more normal federal republican regime with General Eurico Gaspar Dutra as constitutionally elected president. The two principal political parties which emerged were the Social Democratic Party (PSD) and the National Democratic Union (UDN). Both were heterogeneous in composition, but received their direction primarily from upper middle class elements and were correspondingly moderate-conservative in political outlook. The primary difference between them was that the PSD was led by men who had been prominently associated with Vargas in the "New State," while many leaders of the UDN had opposed Vargas.

15. The moderate-conservative Dutra administration failed to cope effectively with the growing economic hardships suffered by lower middle class and labor groups. Partly as a result of this failure, Vargas was able to retain a large personal following and to build up a personal political machine — the Brazilian Labor Party (PTB) — based primarily on organized labor. In the 1950 presidential campaign Vargas exploited both the discontent of lower income groups and the ineptitude of conservative political leaders. He was elected with 49 percent of the popular vote, as against 30 percent for his nearest competitor. However, moderate-conservatives (the PSD and UDN) continued to predominate in both houses of Congress and to control most state and municipal governments.

16. Vargas was no more successful in coping with Brazil's mounting economic difficulties than his predecessor had been. In contrast to the vigor and self-confidence of his earlier rule, his policy was indecisive, largely because of his lack of an assured majority in Congress. Although the PSD generally supported him, it did so at a policy price which tended to alienate his labor-leftist following and its con-

tinued support could not be relied upon. Moderate-conservatives in general continued to distrust him on account of his past record, his labor-leftist associations, his apparent indifference toward Communism, and his known tendency to subordinate pressing economic considerations to the requirements of political expediency. By vacillating between policies designed to gain moderate-conservative support and measures calculated to regain the loyalty of his indispensable labor-leftist following, Vargas forfeited the confidence of both groups.

17. By early 1954 the economic and political situations in Brazil were both extremely precarious. Policies pursued under moderate influence had temporarily averted a foreign exchange crisis, but inflation continued unchecked. With congressional elections approaching, Vargas turned again to the left, the symbol of this decision being a decree doubling the minimum wage regardless of the economic consequences. By adroit politics, Vargas managed to maintain his position despite conservative efforts to oust him on this account, but political tension was raised to such a point that his regime was vulnerable to any political accident. The accident occurred when an Air Force officer was killed by Vargas henchmen who were attempting to assassinate an editor who had been vociferously critical of the regime. The public reaction excited by the Air Force investigation of this affair deprived Vargas of popular support at a time when moderates and conservatives were already out to get rid of him. In these circumstances the Army and Navy acceded to Air Force demands that Vargas be forced to resign.

18. This political intervention by the Army, as the dominant military force, was in keeping with Brazilian traditions. The Army normally remains aloof from politics, supporting the incumbent government, whatever its political complexion, but the Army also considers that it has an overriding responsibility for the preservation of order and of established institutions. It had already warned Vargas, in February 1954, when it demanded and obtained the dismissal of his Minister of Labor. It acted in August, not only in response to Air Force pressure, but also to check the administration's sharp trend to the left and to avert the implicit danger of serious civil disturbances.

The Cafe Administration

19. Cafe Filho's known personal integrity and political independence raised hopes that he might succeed where Vargas had failed in providing effective solutions for Brazil's politico-economic difficulties. Although himself politically left of center, Cafe had come to power with the support of the moderate-conservatives and the military. His cabinet includes representatives of all the principal parties as well as men without party affiliation. For the first time in recent years the Brazilian cabinet is composed predominantly of men of high intellectual and moral character, concerned primarily with the national welfare rather than with personal or party interest.

20. As was the case with its predecessors, the new administration's most pressing problems are economic, particularly the foreign exchange shortage and inflation. It has attempted to meet them by advancing a program of retrenchment and austerity such as no Brazilian government has hitherto dared to propose. Government expenditures have been reduced and government support of industrial expansion has been withdrawn. In large part, however, the administration's retrenchment program has been frustrated by lack of support in Congress. Inflation has not been substantially retarded.

21. The October 1954 congressional elections failed to provide a clear mandate for or against the Cafe program. The moderate-conservative parties retained a combined majority in Congress and could enact the Cafe program if they united to do so. Party discipline in Congress is lax, however. Moreover, party politicians are understandably disinclined to vote for tax increases, credit restrictions, reduction of agricultural price supports, or curtailment of working class benefits in a presidential election year.

The Approaching Presidential Election

22. Party preparations for the presidential election to be held in October 1955 are taking place in unusual circumstances. For twenty-five years Brazilian politics have taken the form of support for or opposition to Getulio Vargas. His death has removed their accustomed point of reference. The labor-leftist elements who followed him are now leaderless, but otherwise moderate politicians are tempted to compete for the labor-leftist vote, realizing that the direction which it takes will probably determine the outcome of the election. On the other hand, the armed forces are taking a greater than usual interest in politics. They are strongly opposed to the election of a Vargas-associated labor-leftist, and, if political developments should tend toward that result, they might intervene to prevent the election of such a candidate.

23. In order to avoid incitement of the masses by competing candidates, and also to ensure the election of a president satisfactory to themselves, the armed forces have favored the idea of a coalition of all major parties in support of a single candidate more or less committed to carry out the policies of the Cafe administration. The UDN has been receptive to this idea. The PSD, however, under the influence of its pro-Vargas wing, has chosen to nominate Juscelino Kubitschek, the governor of Minas Gerais, and to seek a coalition with the labor-leftist PTB. The PTB is not yet ready to commit itself to Kubitschek and the PSD, but could probably be persuaded to do so by proper political concessions. In conjunction with Kubitschek's popular appeal, a PSD–PTB combination would probably be sufficient to ensure his victory in a free election. It might, however, provoke military intervention in the election — unless the military were privately persuaded that Kubitschek, in office, would pursue acceptable policies.

24. The outcome of the election will depend primarily on whether the bulk of the labor-leftist vote can be won by Kubitschek (or any other single candidate), or whether it will be divided among many candidates. The latter contingency is a possibility. Other potential candidates with labor-leftist appeal are Adhemar de Barros, Janio Quadros, and Estillac Leal, representing diverse factions. The election of a moderate-conservative to the presidency of Brazil would be possible only in the event of a serious division of the labor-leftist vote.

25. The action of the UDN will be greatly influenced by the prospect for division of the labor-leftist vote. Against a PSD–PTB coalition, the UDN would be likely to seek a corresponding coalition with Janio Quadros, the independent leftist governor of Sao Paulo. If, however, it appears that the labor-leftist vote will be divided, the UDN might nominate a moderate-conservative with military connections, such as General Juarez Tavora.

26. The next president of Brazil is likely to be a man (such as Kubitschek) committed to pursue labor-leftist policies. The election of such a president would create a political situation similar to that which existed during the Vargas regime. The armed forces would be confronted with a hard choice between condoning further evolution to the left, at the risk of eventually losing their power to act as arbiter in Brazilian politics, or immediately imposing a government to their liking, at the risk of precipitating bitter internal dissension between labor-leftist and conservative-military elements and possibly severe civil disturbances. The prospect, at best, is for continuing political tension in Brazil.

The Communists

27. The Brazilian Communist Party (PCB) lost strength after it was outlawed in 1947. However, since 1951 (when Vargas returned to power), and especially during the last two years, it has had remarkable success in raising funds and recruiting new members. It is now estimated to have 100,000 to 120,000 members and a much larger number of sympathizers. It draws its chief support from urban labor and lower middle class groups, although the leadership of the party is composed largely of professional men and intellectuals. Retired military personnel also have been active in the leadership of front organizations. For the present, the party's primary effort is directed toward the consoli-

dation of its recent gains, rather than toward further expansion. The Communists not only maintain numerous newspapers for the dissemination of propaganda, but have also established an extensive school system for the indoctrination of party cadres. They talk of developing the party in accordance with "the Chinese revolutionary pattern": i.e., by agitation and organization among the peasants leading to guerrilla resistance in the back country and to eventual revolution. Their present strength is concentrated in and around the city of Rio de Janeiro, in the important state of Sao Paulo, and in the strategic "hump" of Brazil.[1]

28. The PCB appears to have two immediate objectives: (a) to stimulate and exploit popular discontent in order to discredit moderate-conservative government, and (b) to stimulate and exploit anti-US nationalism in order to neutralize Brazil as an effective ally of the United States. A good example of Communist technique is the agitation, in conjunction with that of non-Communist ultranationalists, which contributed to enactment of the existing law excluding foreign capital from participation in the development of Brazil's petroleum resources.

29. Vargas was largely indifferent to the rapid revival of Communism in Brazil during his presidency. No Communist sympathizer himself, he presumably supposed that he could control the situation. His indifference, however, permitted intensive Communist infiltration of some labor organizations, and, to a lesser extent, of the bureaucracy and the armed forces.

30. The Cafe administration has taken some action to neutralize this Communist infiltration. Military officers of known Communist sympathies have been retired or reassigned; known Communists among the enlisted personnel are being court-martialed. Communists are also being removed from positions of labor union leadership. As yet, however, little has been accomplished toward removing Communists from the bureaucracy or from elective public office.

[1] The attached map shows more fully the distribution of Communist strength in Brazil.

31. Possibly because the Brazilian Catholic Church underestimates the strength of Communism in Brazil, it has not engaged in a militant campaign against Communism. In any case, Church influence in Brazilian politics is usually weak.

32. Inasmuch as the Communist Party, as such, is still outlawed, Communist political action must be effected through other political parties. The extent of Communist penetration of other political organizations is unknown; it may be extensive in the PTB. In the 1954 congressional election at least five Communists and Communist sympathizers, running under non-Communist party labels, were elected, as compared with one such deputy in the previous Congress.

33. The Brazilian Communists may be able to derive advantage from Vargas' suicide and from his "political testament," which coincided remarkably with the Communist Party line. Their previous condemnation of Vargas has been obscured by their effort to incite a violent popular reaction to his suicide. They now are able to claim him as a martyr to "Yankee imperialism." Furthermore, in the forthcoming presidential election they will be in an advantageous position to push their united front program, auctioning a large bloc of assured votes in exchange for political concessions.

34. For some time to come, the Brazilian Communist Party will probably continue to increase in membership and political influence. It is not likely, however, that the party could, within the foreseeable future, gain sufficient strength to win direct control of Brazil by electoral means or by force. Its influence on Brazilian policy will be exerted through the popular pressures engendered by its exploitation of social discontent and nationalist tendencies in the non-Communist population.

III. THE ECONOMIC SITUATION AND PROSPECTS

35. Brazil has the greatest economic potential of any country in Latin America. Territorially larger than the United States, it has a fast-growing population of about 58 million,

which is about double that of the next largest Latin American republic (Mexico). Although agriculture occupies over two-thirds of the population, only five percent of the arable land is cultivated. Nevertheless, Brazil is the world's largest producer of coffee and bananas, ranks second in the production of cacao and citrus fruits, and is at least in fifth position in the production of sugar, tobacco, corn, and cotton. Brazil's herds of cattle and pigs are fourth largest in the world. Although much of the country remains to be explored, Brazil is believed to have the resources for self-sufficiency in most of the major minerals, the principal exceptions being tin, zinc, lead, copper, sulphur, and coal. Brazil is an important area for US trade (trade both ways in 1953 was approximately $1.1 billion) and for direct investment of US private capital. By 1953 such investment totalled slightly over $1 billion.

36. Brazil's economic growth since 1930 has been rapid. Since the end of World War II gross investment has amounted to about 16 percent of GNP annually, the overwhelming proportion of which has been devoted to industry and construction. GNP increased about five percent annually from an estimated $10.8 billion in 1950 to $12.5 billion (at 1950 prices) in 1953. By 1951 the manufacturing sector (including construction) had come to contribute 24.5 percent to total GNP, thus equaling the contribution made by the agricultural sector. Brazil has continued, however, to rely overwhelmingly on agricultural and animal exports for foreign exchange earnings. Such exports, except during World War II, have accounted for well over 90 percent of Brazilian exports, with coffee contributing between 40 and 70 percent. (Brazil normally supplies about one-half of US coffee imports, thus acquiring the foreign exchange which has permitted Brazil to become one of the important American markets for machinery and vehicles. During 1953 and 1954 Brazil supplied only 40 percent of the US coffee market, however. In the latter year the decrease was particularly serious for Brazil, since total US coffee imports were off 19 percent under the impact of an unprecedentedly high coffee price.)

37. Divergences in the rate of growth between the various sectors of the economy have given rise to serious maladjustments. Rapid industrial expansion has not been accompanied by a proportionate development of transportation and power facilities. Agricultural and mining production for export has been neglected in favor of manufacturing industries. Moreover, emphasis upon capital goods industries within the industrial sector tended to create an imbalance between the supply of and effective demand for consumers' goods. Inadequacies in basic productive facilities and high cost of distributive services contributed to high unit costs of consumer goods, maintained and encouraged by a deliberate policy of protection through tariff and foreign exchange regulations.

38. The rapid growth of the Brazilian economy has occurred under conditions of uninterrupted inflation. In the last 15 years the cost of living has been increasing at an annual rate of more than 16 percent; in the first 11 months of 1954 the cost of living rose 22 percent. Prices at the end of 1954 were about 770 percent above those for 1939. This rate of price increase is of a different order of magnitude from that historically experienced by Brazil, namely, about 2.5 percent annually. In general, wages have lagged behind prices. The inflation has been the result of several factors. For some years prior to 1947, it was stimulated by the accumulation of substantial foreign exchange surpluses, which Brazil was unable to convert into consumers' goods. Since 1947, domestic factors such as government deficits and the expansion of credit have fostered the inflation. Of considerable importance also has been the fact that a large proportion of investment was of the long-term variety which did not result in an increased output of consumer goods.

39. Brazil's effort to maintain the rate of industrialization, even at the cost of severe inflation, has led to recurrent foreign exchange shortages. In order to permit domestic industry to purchase its needed imports cheaply, a highly inflated value for the cruzeiro was maintained. This over-valuation caused a weakening of the competitive posi-

tion of Brazilian exports and a concurrent loss of foreign exchange. At the same time expansion of industry stimulated Brazil's demand for raw materials, capital goods, and fuels, most importantly petroleum. Although industrial production was able to provide significant foreign exchange earnings during World War II, during the postwar period it was unable to compete with the older industrialized countries, in part because of the overvaluation of the cruzeiro. In the same manner, although the Brazilian Government has insisted in recent years that new foreign investment be "constructive," it has given greater emphasis to further industrialization than to investments that would produce foreign exchange. Consequently the drain on foreign exchange resources caused by Brazil's rising industrial production has been unmatched by new foreign exchange earning power.

40. Brazil's foreign exchange difficulties are dominated by the large and increasing demand for fuel imports. About one-third of anticipated 1955 dollar receipts are allocated to petroleum imports. The wisdom of securing foreign capital to find and exploit the domestic petroleum resources, which have been inferred from Brazil's geological structure, has long been recognized by many prominent Brazilians, in view of the lack of good coal reserves and poorly located hydroelectric resources. In 1953, however, extreme nationalists and Communists spearheaded passage of legislation establishing a government petroleum monopoly and excluding foreign capital, and they have since prevented a modification of the legislation by the new administration. Brazil's monopoly is not likely to succeed except, perhaps, over the long term, because of the country's lack of funds and technical skill. Yet, in the absence of indigenous fuel resources, further economic growth will place increasing strains on the already inadequate foreign exchange resources.

41. During 1953 a serious attempt was made to meet the foreign exchange problem. Early in the year the Vargas administration was faced with a foreign exchange crisis and a large commercial debt backlog, which was temporarily resolved by a $300 million Export-Import Bank loan. Shortly thereafter a new Finance Minister, Oswaldo Aranha, attempted to reorient the economy to eliminate some of the obvious causes of disequilibrium. He made a determined effort to stimulate exports by providing subsidies and exchange incentives. Simultaneously, he initiated a foreign exchange system which restricted the volume of all imports, but especially the less essential ones. Particularly important was the preference given through exchange control to the development of the retarded basic service industries such as transportation and power. Aranha failed, however, to secure adequate executive or congressional support. The executive branch feared that a curbing of inflation with the consequent restriction of industrial development would seriously undermine Vargas' already weakened political position. The Congress, on the other hand, refused to accept the political risk involved in opening Brazilian oil to foreign investment. Both Congress and Vargas apparently hoped that large coffee exports at favorable prices would postpone or eliminate the problem of drastic internal economic readjustment.

42. However, coffee prices weakened in May 1954, seriously aggravating Brazil's economic position. Vargas then attempted to peg the price of coffee, a move which resulted in a serious curtailment in Brazil's volume of exports and earnings of exchange. Commercial exchange obligations once again rose to serious proportions. At the same time inflation was permitted to run, fed by treasury deficits, expansion of bank credits, and the *de facto* devaluation of the cruzeiro. The price-wage spiral was put into motion once again by a series of wage increases, particularly by the doubling of minimum wages decreed by Vargas as of 1 May 1954.

43. The Cafe administration has demonstrated its awareness of the necessity for politically unpalatable measures to meet Brazil's economic difficulties. However, it has not felt itself sufficiently strong politically to propose such basic reforms as restriction of wages, abandonment of coffee

stabilization, or the admission of foreign capital for petroleum development. Moreover, congressional cooperation has not been forthcoming.

44. On taking office the Cafe administration was immediately faced with a foreign exchange crisis which was met with the help of a $200 million loan from US banks. At the same time it undertook a program to raise exports and reduce imports, particularly in relation to the dollar area. The trade pattern planned for 1955 provides for imports from convertible currency areas (primarily the US) in the amount of $532 million, a sharp decrease from the $755 million of 1954. The machinery for implementing this decrease lies in a purely administrative reduction of the dollar exchange auctioned to importers. Such a reduction is probably feasible since some imports can be shifted to the nonconvertible account where there is little payment difficulty except in connection with sterling. Exports to the convertible currency areas are to be raised from $580 million in 1954 to $720 million in 1955. Brazil's recapture of its traditional share of the American coffee market will be essential to the realization of this export goal.

45. The major deterrent to adequate coffee sales in the past eight months has been the price stabilization program instituted by Vargas in the last months of his regime, with nationalist overtones of "protecting" Brazilian coffee interests from "international financiers." Under the program a minimum export price was established, and the Bank of Brazil granted to coffee interests loans equaling 100 percent of the value of the coffee stocks, valued at the equivalent of a New York price of 87 cents per pound. When the policy was instituted it was hoped that the New York price would be forced up. In fact, it has decreased about 33 percent, mostly in two stages, in August 1954 and February 1955. Meanwhile the coffee interests are still receiving the same minimum cruzeiro price and are under no financial pressure to dispose of their stocks, and foreign exchange receipts from coffee sales are running below Brazil's minimum requirements. As a result of this, Brazil was forced to seek new financial aid early this year. On 9 February 1955 the Export-Import Bank granted a $75 million credit which Brazil may draw on at the rate of $15 million monthly, if necessary to meet the estimated minimum dollar exchange requirements. International financial commitments in dollars, which cannot be further postponed, require foreign exchange earnings (including drawings under the new $75 million Export-Import Bank credit) of at least $60 million monthly; such earnings can be obtained only from exports of coffee to the United States in greater quantity than in January. If this does not take place, the use of cash balances and existing borrowing rights from private American banks might close the gap for a short time, but subsequently Brazil would again seek US Government aid. The Brazilian Government may believe that American exporters, alarmed at the loss of their markets in Brazil to European firms unaffected by the dollar shortage, would successfully press the US Government to grant effective financial aid.

46. The Cafe administration recognizes the need to check inflation, but, in the existing political situation, the courses open to it are narrowly circumscribed. It has restricted bank credit. It has also proposed new taxes in order to reduce its deficit spending, but could obtain from Congress only one-third of the tax increase requested. It thereupon undertook to reduce government expenditures, but has actually been obliged to grant to its civil and military employees "temporary" pay increases not provided for in the budget. Moreover, the Brazilian Government is responsible, in the public mind, for the country's continued economic growth, and is therefore under heavy pressure to maintain a high rate of economic activity. A continued decline in the rate of private investment, such as occurred in 1953–1954, would probably compel the government to resume expenditures for public works, even though it is fully aware of the inflationary effects of such a policy. Consequently, there is little prospect that the Cafe administration can substantially retard the progress of inflation.

47. In these circumstances (paras. 43–46) the Cafe administration cannot be expected to accomplish much toward the solution of Brazil's deepseated and politically dangerous economic difficulties. The administration to be elected in October 1955 will have to face the same problems. There is little prospect that it will have the political strength to impose drastic remedies. In fact, as long as any Brazilian administration assumes that dollar loans are readily available, there is little likelihood that it will incur the political risks involved in stabilizing the economy. However, the administration would be even less willing to follow politically dangerous policies in the absence of dollar loans. Rather, it would be under extreme pressure to apply radical, nationalistic solutions to Brazil's economic problems. In any case, effective action over an extended period will be required to stabilize the Brazilian economy.

IV. THE ARMED FORCES

48. The Brazilian armed forces, organized and trained on US lines, have an over-all strength of approximately 204,000. The Army, numbering 108,000, consists of 7 infantry, 1 armored, and 4 cavalry divisions, numerous separate combat units, and supporting troops. In addition, there are 55,000 militarized police available for local and regional use. The Navy, with a personnel strength of 21,000, has a combat force of 2 light cruisers, 7 destroyers, and 32 smaller escort, patrol, and mining vessels. Two additional destroyers now under construction may become available during 1955. The Air Force, with a personnel strength of 20,000 (including about 1,000 pilots), maintains 5 fighter, 2 light bomber, 2 patrol, 2 reconnaissance, and 2 transport squadrons. It has about 950 combat, reconnaissance, and transport aircraft, including 68 British jet fighters.

49. The operational effectiveness of the three combatant services is high by Latin American standards as a result of their reorganization, re-equipment, and operational experience with US forces in World War II, and of the assistance of US military missions. Their effectiveness is impaired, however, by a lack of adequate support facilities, poor maintenance and general obsolescence of equipment, and dependence on foreign sources for resupply of material, munitions, and fuel. A severe dollar shortage and the high cost or unavailability of US military supplies have caused Brazil to turn to Europe for some aircraft and military equipment, to the detriment of Hemisphere arms standardization. However, procurement from this source is also severely limited by fiscal considerations.

50. Brazil participates actively in the Inter-American Defense Board and has a bilateral military assistance agreement with the US. Under this agreement, Brazil has designated certain units as available for Hemisphere defense, including service outside its own national territory. With MDAP support, the equipment and training of these units will be improved.

51. The Brazilian armed forces are adequate to maintain internal security and to deter aggression by any neighboring power. They could not repel a major overseas invasion without US assistance. In the event of general war they could probably protect strategically important installations and facilities from extensive sabotage and from possible raids. The Brazilian Navy and Air Force have limited convoy escort and antisubmarine warfare capabilities, but effective patrol of the long Brazilian coast would require the active participation of US forces. With US logistic support the Army could provide a small expeditionary force.

V. PROBABLE FOREIGN POLICY

52. Brazil has traditionally regarded itself as the particular friend and ally of the US in Latin America. With a self-confidence based on its vast extent and relative political stability, it has considered itself superior to its Spanish-speaking neighbors and the natural associate of the US. Moreover, the US is by far Brazil's most important coffee market and the only important source of needed financial and technical aid. For these reasons Brazil strongly desires the friendship and support of the US and is highly sensitive to any US tendency not to accord Brazil special consid-

eration and favor. At the same time Brazil is sensitive to any implication of US tutelage.

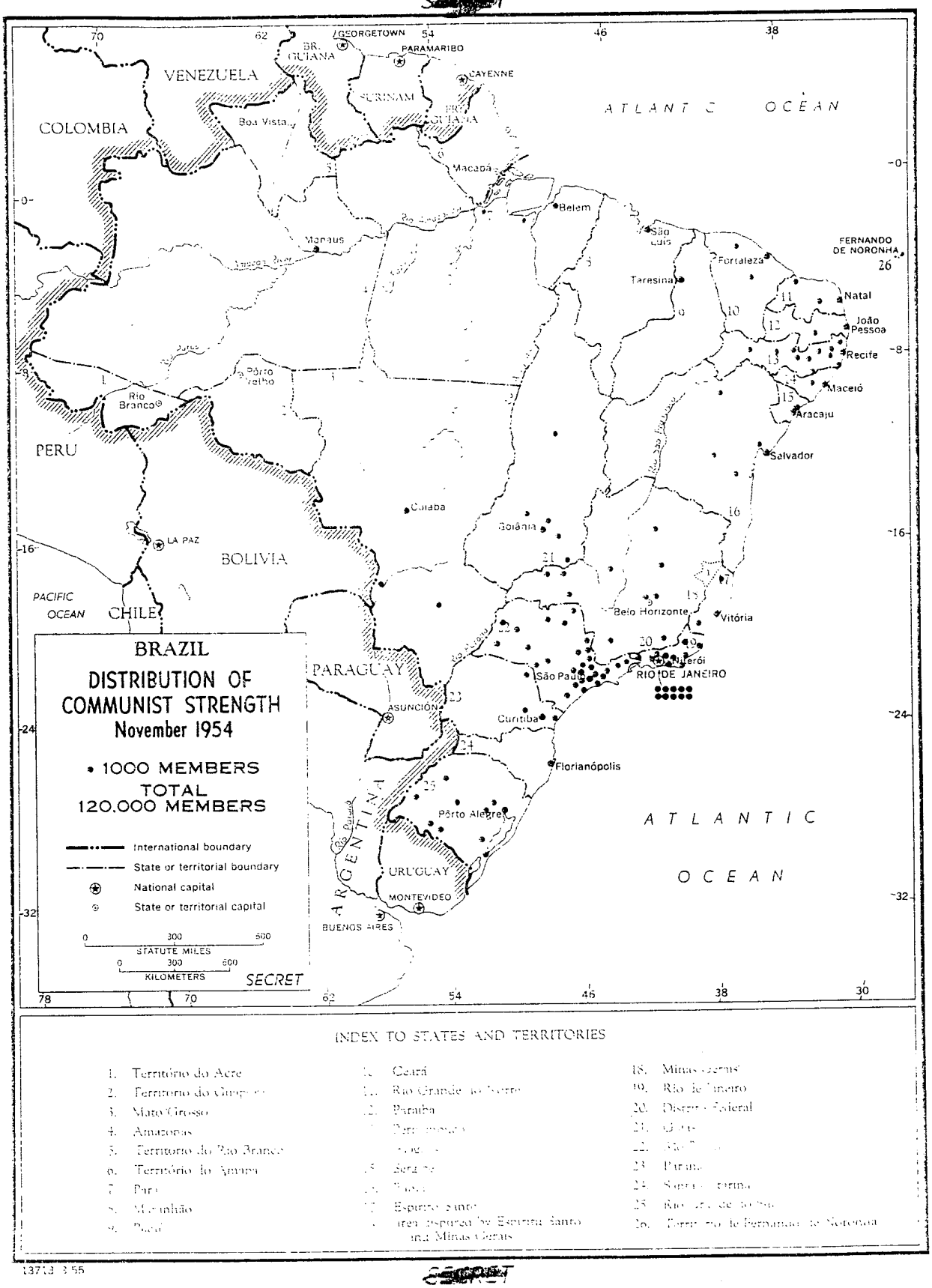
53. In recent years US–Brazilian relations have occasionally been impaired by growing Brazilian nationalism, which has produced friction in both economic and politico-military affairs. An important factor in this development has been a growing feeling in Brazil that the US undervalues Brazil's friendship and tends to take it for granted. In particular, Brazilians feel that US economic and financial assistance to Brazil has not been commensurate with Brazil's past services and present strategic importance to the US, or with Brazil's value to the US as a moderating influence in Latin America and in UN affairs. In common with other Latin Americans, Brazilians resent what they regard as the favored position of Europe and Asia respecting the amount and terms of US assistance.

54. Brazil has made no move to restore diplomatic relations with the USSR which Brazil severed in 1947. It maintains diplomatic relations with Poland and Czechoslovakia and has received a commercial mission from Hungary. Brazil's trade with the Bloc has increased markedly over the past year, but is still very small. There are mounting popular pressures for expanding relations with the Bloc. This idea is generally attractive because of Brazil's need to find new markets for its exports, and also probably at official levels as a means of strengthening Brazil's bargaining position vis-a-vis the US. Communists and their sympathizers are pressing the idea of large Bloc markets for their own ulterior purposes, with considerable nationalist support.

55. In the Latin American community, Brazil has always opposed Argentine bids for leadership. In particular, it has sought to counter Argentine designs on Uruguay, Paraguay, and Bolivia. Fundamentally, Brazil deprecates the idea of competing blocs in Latin America, and promotes instead the concept of Hemisphere solidarity.

56. Brazil's political and military leaders favor the concept of a collective Hemisphere defense, and they also seem opposed to neutralist positions in connection with broader international problems. In event of general war, Brazil almost certainly would participate actively in support of the US.

57. Brazil almost certainly will continue to support the US on major issues between the US and the Soviet Bloc. Barring an increase in the influence of the Communist and extreme-nationalist factions in the Foreign Office, Brazil will almost certainly continue to support the US on most important issues in Hemisphere affairs. Brazil's strategic materials will continue to be available to the US and it is likely that progress on the large-scale manganese development in northeastern Amapa will permit shipments to the US to begin in early 1956. However, a desire to strengthen its bargaining position vis-a-vis the US will be an important factor in Brazilian peacetime diplomacy, and frictions will almost certainly continue to occur, particularly on economic questions. Brazil will seek to establish closer economic relations in Latin America and with Western Europe, and will also seek to increase its now minor non-strategic trade with the Soviet Bloc.



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